Economic Analytical Notes, 2003

Economy overview at the beginning of the year

by Anatol Gudim

The new year of 2003 has begun with the Government ***sizing up of the previous year***. Positive estimates prevail. It is the third year in a row when the Republic of Moldova registers GDP growth (7.2% in 2002 and altogether during the “triennial period of growth” of 2000-2002 – 16.4%); industry and agriculture growth was correspondingly 10.6% and 3.0%. Nevertheless, share of services within the GDP structure is much larger than share of the production sphere; while 70% of budget incomes were provided by the customs. The Government lays a particular emphasis on social character of its actions: average monthly wage increased by 32.3% and reached 666,4 MDL and average pension – 168 MDL. For all that minimal basket of goods in December 2002 was officially estimated as 1177 MDL. The National bank has played its traditional role as the key structure that stabilizes macroeconomic situation through providing for stability of the Moldovan lei (13,5 MDL for 1 USD in 2002 as compared to 12,9 MDL in 2001) and inflation of only 4.4%. Monetary reserves of the National bank have been raised up to 264 mil USD through purchase of currency transferred into the country by the Moldovan citizens working abroad inclusively (more than 200 mil USD in 2002).

But some facts can put one on guard: internal and external state debt has increased; export was 1,6 times smaller than import; investments – a precondition for the future – grew only by 4.0%, which is less than GDP growth; the state did not obtain from privatization even a tenth part of what was planned during the budget approval; business environment still remains unfavorable.

Majority of the population, according to opinion polls, evaluated positively tendencies of the country’s socio-economic development and actions of the Government. These actions, however, in spite of their abundance (circa 30 strategies, programmes and concepts) were focused mainly on solution of current issues. This was also reflected by a record number (about 1800!) of Government decisions on different issues of public management made in 2002.

But there is an overall impression that the present Government (even after almost two years of its activity) has not succeeded yet in determining the degree of “state regulation” (leitmotif of its starting Programme, April 2001) and “freedom of market mechanisms action”, especially in the sphere of entrepreneurship, which is the market economy driving force, while private sector provides for almost 85% of GDP. Lack of clarity and contradictoriness of the Government economic policy are main causes of its long-drawn “haggle” with the IMF and the World Bank regarding further loans. Thus, the second SAC-III transfer instead of November-December 2002 will be rendered to Moldova in April at best.

On the whole, regular activity of the Parliament and the Government, ***macroeconomic tendencies and current events of January-February of 2003*** still follow trajectory of the last year. Among laws that joined into force since the beginning of the year are: on migration, on additional social protection of pensioners, on public communal services, on petitions, on copyright. There were introduced amendments into the laws on education, on state regulation of external trade, on procurement of goods, work and services for state necessities, on sanitary-and-epidemiologic protection of the population, on payment for pollution of the environment.

The Government issued during January-February almost 200 decisions, including decisions on approval of the Unified programme for compulsory medical insurance (which is being introduced since July 1, 2003) and of the Concept of corporate management of enterprises. It seems that the Government responding to the directive expressed in the Parliament by the President V. Voronin on "modernization of state management, liberalization of the economy and activization of civil society resources" (according to the monitoring of 9365 documents registered by the State Chancellery) issued decision on results of execution of normative acts, decrees and commissions of the President of the Republic of Moldova in 2002 by central public management bodies (#126, 10.02.2003), which points to "indifference and irresponsibility of persons bound to execute them" and that "leadership of central public management bodies became less exigent towards responsible officials", etc.

Events ***in the real economy and social development*** meanwhile took their normal course. The Department of Statistics registered in January, 2003, that industrial production grew by 13% and inflation index – by 1.9%. State budget as regards incomes was executed by 125%. It is important that an international agency – Fitch Ratings – raised Moldova's long-term external obligations rating from "DD" (risk of default) up to "B-", i.e. up to the indicator that now is attributed to Uruguay, Lebanon and Gambia (Moldova had such rating in 1999 after the Russian/regional financial crisis).

Year of 2003, unlike other previous years, began in expectation of positive changes in solution of the "Transnistrian problem" and, hence, in rapprochement of economies of Moldova and Transnistria. The causes were both the idea of federalization of a "common state" proposed in Kiev by the OSCE and guarantor-countries, decision of the OSCE summit in Porto on removal out of the region of the Russian military equipment till the end of 2003, as well as new tendencies in Transnitria's economy – beginning of a monetary privatization of enterprises, referendum on private property for land, changes in social policy, etc. And, finally, on February 10, 2003, there was published declaration of the President V. Voronin on a new initiative – plan of a definitive settlement of the Transnistrian problem to the extent that a new Constitution of the country will be elaborated and passed jointly, given the lack of which "Moldova's people cannot improve radically its life and restore its economy and social sphere".

"Socially oriented market economy" as a model for construction in Moldova was designed by the present Constitution, active since July 29, 1994. The Government, according to this guideline and in collaboration with the IMF and World Bank, at present finishes (deadline – March 2003) elaboration of the ***Strategy of economic growth and poverty reduction*** (PRSP). Such strategies are being realized in more than 40 poorest countries of the world; they serve as a road-map for those countries in realization of economic policy, while for international organizations they serve as a framework document for monitoring of situation in a given country.

Therefore quality of the PRSP-Moldova will be evidence of the present Government professionalism, of its preferences regarding not only state dirigisme and intentions to liberalize economy, but its openness to collaboration with official structures, with the opposition and civil society as well.

Prognosis of the Government for 2003 is quite optimistic: GDP growth – 6%, average wage growth – 20%, inflation – 6.0%, national currency exchange rate – 14,6 MDL for 1 USD, state budget deficit – 0.8% of GDP. International organizations are more discrete: they expect 4.0% GDP growth, further increase of external and internal debt and worsening of trade balance, assuming that sustainable economic growth can be achieved only through speeding up structural reforms and business barriers. Another emerging problem is "improvement of the country's administrative-territorial system". One can foresee that return from 10 to 33 smaller territorial units will not only cost more as regards management expenditures, but will also make work of the Government more difficult as regards both interaction with the new local administration and execution of the budget, relations with business environment, quality of statistics, etc.

Under all these circumstances ***quality of governance*** will continue to be in 2003 the main concern for authorities, business and population. According to estimate of the President V. Voronin "the present structure of the executive power does not comply with objective programme tasks of the state" (session of the Parliament, 30.12.2002); "we need a well coordinated government team, experienced and vigorous" (session of the Government, 17.02.2003). Indeed, if one takes a look at causes of slow and inconsequent reformation of the economy and periodic attempts to return to methods of administration, then they can be explained in many respects by unreformed state management machinery. It is worth paying attention to both excessive number of ministries, departments and agencies at the higher (central) level – more than 50 – and lack of a strong center of elaboration and coordination of economic policy. The Government does not act as a single team, but rather as a conglomeration of representatives of different group interests. This situation hampers quite effectively all attempts to liberalize Moldovan economy.

It is recognized that formation of a new government is the best time for realization of deep changes in structure and functions of state machinery. If this takes place in 2003, then it is expedient to take into account experience of other European countries, including: distinct division of political posts in the Government (prime-minister, ministers and their deputies, councilors) from apolitical state service (all other posts); competitive selection of candidates for state posts; creation of necessary conditions (labor remuneration, education and skills improvement system) for the sake of stability of employment in the state service; ethical conduct code for officials.

Instead of passing new normative acts, majority of these measures requires changing of those acts that already exist or can be realized within the framework of present authorities of the executive power.

Economy: events & commentaries

by Anatol Gudim

In the last couple of weeks economic issues were the major concern of the country leadership, representatives of international monetary organizations, and economic media outlets. Judging from a multiple perspective, one may conclude that there are major risks at stake as far as economy is concerned, but there are opportunities as well. Let's closely consider them.

Two months of the year already elapsed, but it is still not clear whether the Government would secure *much-awaited assistance from IMF and World Bank* for its activities? The two representatives of the said institution (E. Ruggiero, C. Elbert) hosted one after another press conferences in February and both of them reconfirmed IMF and WB commitment to provide assistance to Moldova, on condition Moldovan authorities meet the requirements stipulated in the previously agreed structural reforms program and establish a favorable business environment in the country. Indeed the said requirement may not be fulfilled all at once, however donors are mainly concerned by the frequent "non-market" initiatives of the Government (like changing the laws, introducing subsidies for the agricultural sector, limiting the exports, thwarting privatization process, etc).

Much-awaited IMF mission (M. Castello-Branco) would arrive in Chisinau only on March 13. However a mission of the WB (I. Hoffman) is currently in Moldova monitoring the elaboration of the Poverty Reduction Strategy. If positive $ 142 million might flow into the country for PRSP enforcement. Meanwhile, the state budget is highly volatile, especially as the salary payments are concerned. For instance the country's major intellectual center – Academy of Science – received its last salary in December. In an attempt to resolve the problem, Ministry of Finance allocated 18,6 million Lei ($ 1,3 million USD) incurred from the sale of T-bills to commercial banks to cover the budget deficit for January – February.

In the meantime, in February Ministry of Economy released its *far-more optimistic macroeconomic forecasts for 2003*: 7% GDP growth (initially forecasted 6%); 10% industrial growth; 9.6% exports growth; and 11% salary raise. Needless to say, agricultural growth has been surprisingly decreased from 5% to 2%. The decrease was probably determined by President's negative evaluation of the "catastrophic" situation in the agriculture. Production cooperatives were recommended as a last-ditch method to recover the agriculture, by reorganizing and exempting them from taxes.

In a related note, President Voronin indicated that the greatest achievement of the last two years was the industry recovery "privatization had lead to de-industrialization, whereas we have started to industrialize the country step-by-step, enterprise by enterprise, despite the lack of investments". Indeed, after 1995 the great majority of industry, except for machinery construction, managed to adjust to the market economy, mainly due to the foreign investments (CMC-Knauf, Ciment-Rezina, Glass Company, Ionel, Balteanca, Floarea Soarelui, etc – a total of 80 enterprises). Currently, industry and services are the ones pooling stabilization of the economy.

As energy accounts for one third of the foreign debt and for the considerable price of the production and services, the Government started a new round of negotiations with Gazprom on lowering the tariffs to $50 USD per 1000 m^3 (currently $80 USD per 1000 m^3). An agreement was reached that free-lance producers (ITERA from Kazakhstan) would deliver 1,300 million m^3 of gas at $61.5 USD per 1000 m^3. Other initiatives: Ministry of Energy suggested developing a network of mini-power stations, as well as the intention of the „Danube-Balt-Trans" Russian-Moldovan joint venture to build by April 1 a temporary wharf in Giurgiulesti, able to receive 6,000-10,000 tones of petrol per month.

As usual, Government agenda included the approval of numerous concepts and programs, such as: national policy in the field of aqua resources; renewal of heating system; road management, etc; as well as social issues, such as: obligatory medical insurance; payment of indemnities to the deposits in the Savings Bank; efficient administration of state housing, etc. Needless to say, there are some Government resolutions pointing to the poor enforcement of its decisions by state administration. An illustration of this is the failure to gather the income declarations from state officials in due term, the deadline being extended until July 1, 2003. Another example is the Decision on enforcing the Government Resolution "On fighting illegal passenger traffic no. 1054 of 08.05.2002" (February 26, 2003) reading that the decision had not been enforced, consequently a new deadline for fighting embezzlement and corruption was set.

Given President Voronin's statement that Moldova's economy would boom only if Transdnistria is reintegrated, a special consideration should be given to the activity of the recently established Ministry of Reintegration. The Ministry took part in the negotiations on Transdnistria under the auspices of OSCE (Tiraspol, February 27-28) and came up with several initiatives on establishing a Free Trade Zone "Nistru" with the support of Chinese investments. Meanwhile, Transdnistrian authorities set new customs tariffs on import and simplified the taxation from 10 to 1 tax for small business (commencing April 1), practice which although debated for a long time in Moldova has not been implemented yet.

Republic of Moldova has been in the spotlight of foreign media outlets as well. "*The Economist*" (edited since 1843), a well known political and economic magazine, featured an article *Europe's failed state* in its February 13 - 20 issue, presenting Moldova's economic situation as quite gloomy, even recommending outside administration of its financial sector. Ministry of Finance commented on the article: "the writer's findings are politically motivated, subjective and provocative, and were not supported by any realistic arguments".

It is worth mentioning that since mid-1990 *The Economist* published at least a dozen of articles on Moldova, with one of the first ones in March 1995 presenting the country as "laboratory of right reforms". The articles to follow were more and more gloomy: "Nowhere land", (June 1999); "Can Moldova Get Worse?", (July 2000); "The Land That Time Forgot", (Sept 2000); "Cold Christmas in Moldova", (Dec 2000); "A New Misery Curtain", (June 2001); "The Future of Europe's Must Dismal Country Looks Ever Bleaker", (April 2002). Former Prime-Ministers Ion Sturza (1999) and Dumitru Braghis (2000) complained about such a bad coverage. *The Economist* published their comments under the *Letters Column* but stayed on its position. The negative outlook on Moldovan reforms has been even further enhanced by the "unreformed and unapologetic communists back to power", but then what else might authorities expect from such a “bourgeois magazine”? Needless to say, *Economist* published its article on Moldova at the time another well-known magazine; *BusinessWeek* featured a “promotional article” about the Republic of Moldova presenting the situation in a more positive light (for further details see www.vegamedia.com).

On the other hand, *The Economist Intelligence Unit* producing for more than half a century economic analysis and forecasts on over 200 countries, provides in its latest (35 pages) review on Moldova a more promising forecast: “real GDP growth should remain moderately strong in 2003-2004” (for further details see www.store.ein.com).

Financial challenges lying ahead of Moldova in 2003

by Adrian Dumitriu

Recently Ministry of Finance has confirmed some earlier forecasts on the *financial challenges lying ahead of the Republic of Moldova in 2003*, in particular budget enforcement. Although at the time 2003 budget had been worked out it was already clear that some problems would eventually surface, the Ministry preferred to neglect them and adopted a budget, which right from the beginning was labeled as a too optimistic, due to its virtual revenues forecasted from privatization, exaggerated foreign aid and high expectations as far as expenses are concerned.

Ministry of Finance's report published in "Moldova Suverana" (governmental newspaper) highlights some contradictions: on the one hand it praises the effectiveness and cooperation in enforcing the budget, and on the other the very same effectiveness is blamed for the situation Republic of Moldova has found itself in, which in its turn determined Minister of Finance to alert on the financial challenges in 2003.

Preliminary reports *on the budget enforcement* released by the Ministry of Finance for the first months of 2003 indicate an increase in the revenues to the state budget. It is worth mentioning that the reported increase is compared to the "same period of the last year". However, the latter was characterized by stagnation in foreign trade (both import and export). A number of importers from Moldova anticipated the introduction of pre-shipment inspection and imported huge amounts of goods in November - December 2001, whereas the normal trade resumed only in March - April 2002, when the inspection procedures became clear. This was also confirmed by the data released by the Customs Department reporting high revenues in January -February 2003 as compared to the same period of 2002. Again increased foreign trade (both in value and in number of import - export transactions) accounts for the boosted Customs' revenues.

There is another explanation for the increased revenues as compared to the same period of the last year, namely evolution of exchange rates vs. *national currency*. This refers in particular to the considerable fluctuations of Euro vs. MDL, some of the excises and customs taxes being calculated in Euro whereas levied in MDL. In early 2003 one Euro was around 16 MDL, whereas in the same period last year it was around 11 MDL.

Even if domestic and foreign developments are favorable for levying higher revenues to the state budget in nominal terms, it is claimed that rather the boosting business accounts for it. Cases have been registered of *fiscal administration* by imposing businesses to make the payments to the state budget in advance or by means of the newly-established Center for Fighting Economic Crime and Corruption, which is persecuting even the businesses that comply with the law. It seems that domestic business, regardless of its field of activity, is confronted with more and more legal or other constraints raised by the state.

To a large extent the enforcement of 2003 budget would depend on whether *international monetary organizations* would resume funding Republic of Moldova. Although troublesome, negotiations in this respect might bring 10 million USD from the World Bank and 15 million from the EU. This would enable the country to service its foreign debt. Further, if foreign aid is not resumed it might impact financial markets, interest rates, fluctuations on exchange market and inflation rate in 2003. It seems that the seasonal character of national currency depreciation is taking a longer period, while resumed external funding would reduce its further depreciation.

Furthermore, if the foreign funding is not resumed, the temptation to directly borrow from the National Bank of Moldova would be much higher, although neither the Law on the State Budget for 2003, nor monetary policy provide for such borrowing in 2003. *Inflation pressure* has become too obvious in the first months of 2003.

Debates on economic, customs, currency and other kind of unions have been recurring both domestically and abroad lately. I would like to dwell on the customs union by pointing that *the stability of national currency* relies on a number of economic as well as psychological (behavioral) factors. That is, any doubt in the future of the Moldovan Lei (including whether it would be still in use) may lead to some negative outcomes, like depreciation of the Lei (although there would be no economic grounds for such depreciation). A clear message from the authorities, including the monetary ones, anticipating (rather than mere ascertaining) the developments, should calm the spirits to a certain extent.

Year 2003 may be by all means characterized as tough from financial point of view. The last ditches on a short term are foreign creditors. However, they would not guarantee stability in the long run. Worsening business environment and foreign debt burden would continue to destabilize Republic of Moldova economic policy as long as there would be confused, contradicting and chaotic messages and initiatives in the field of economy.

Social orientation: no strategy yet?

by Stefan Zgama

Since the beginning of 2003 two additional factors have drawn increased attention to social issues, which the Government has constantly declared as its priority. Firstly, elaboration of the Poverty Reduction Strategy (for which the country wishes to receive World Bank and IMF credits). Secondly, necessity of a "bigger care for people" on the eve of local elections. That is why, at least half of the 400 Government decisions adopted in January - March were on social issues.

In this respect, emphasis has been placed upon strengthening state regulation in the field of employment, wages and social security. Thus, beginning with April 2003, the pensions of 658,000 pensioners will be raised by 18%. The Government passed this decision given the increase of the minimal wage, which in its turn should secure higher revenues to the state social insurance fund.

In March, the National Employment Program for 2003 - 2005 was finally approved. The situation of the labor market in the country is quite worrisome. The decrease in the population number registered since mid 90' has been intensified in the recent years by the decreasing number of population able to work (ranging 18 - 62 years of age), in the IV quarter of 2002 they accounted for 1,579,000. According to statistics the latter reside mainly in rural areas, where 60% of the unemployed live. Resumed economic growth (in GDP terms!) had no impact so far on the employment: 1,688,000 in 1993 and 1,505,000 in 2002 (a 10.8% reduction). Under the methodology of the International Labor Organization, there were 110,000 unemployed and the unemployment rate was 6.8%. Youth, including those with higher education, accounts for the great majority of this figure. Half of those who went abroad in search for a job are younger than 30. The National Employment Plan provides that 70 "actions" would be organized to create new workplaces, to facilitate employment, to aid youth in finding jobs, to conduct professional training, to organize public works and to ensure social protection of the unemployed. The goal is to reduce the unemployment rate to 6.0 - 6.1% by 2005.

Government decided that the time has come to increase the monthly wage rate for the lowest (first) qualification rank workers in self-financing enterprises from 250 to 300 MDL. And since June 1 it will be raised for the second time - up to 340 MDL.

Gradual increase of the minimal wage sounds encouraging. However, a guideline, instead of inflation rate, should be rather considered adjustment of the minimal wage to the cost of living (in the IV quarter of 2002 - 521.7 MDL). So far, the ratio is 0.5:1.0. It is worth mentioning that the minimal wage of the public employee is currently 100 MDL, or 19.2% of the cost of living. Public employees' wage has been a constant headache for the Government. In 2002 monthly wage in education was 464.2 MDL, or 67.1% of the average salary per country, in health-care and social services 463.3 MDL or 63%. The Government recommended raising the wage in the budget-financed sphere by 15-20%, however trade unions believe it is not enough. The

Government declared it would raise the wage despite the fact that its arrears in paying wages to the budgetary sphere exceed 170 million MDL (approximately 12 million USD).

Republic of Moldova is considered to be one of the poorest countries in Europe. So who are poor, where do they reside, and what stratum is the most affected by poverty? According to the "Report on Poverty" developed by the Poverty Monitoring Unit of the Ministry of Economy poverty rate has been estimated at 22.8%, based on the relative poverty line - 50% of the average household consumption, i.e. every forth Moldovan may consider himself to be relatively poor. This conclusion has been made based on examination of 6,400 household budget surveys (2002).

Poverty level is a little higher in the South of Moldova, where agriculture and small towns are predominant. In general, residence in rural areas is a factor increasing the risk of poverty (poverty rate is higher in villages than in cities). As for small towns, unemployment is stagnant there, many "old" factories are not working and there are no investments to create new work places.

It is interesting that in contrast to many countries, in Moldova the poverty is lower in households lead by women than in those lead by men. At the same time it was pointed out that the younger the women are, the lower is the risk for the household to become poor.

In general, the young age of the household head, which is considered to be a risk factor in other countries, is not valid for Moldova. Moreover, the poverty among the households lead by young people, up to 30 years of age, is lower as compared to other families and represents 72.1% of the average level. The reason for this is the fact that traditionally young families benefit of material support from their parents and relatives, which enables them to enjoy better living standards especially until they have children.

The Government should pay attention to the fact that poverty in families increases with the number of children. The poverty rate in families with three children is 1.4 times higher than in families with one child, whereas in families with four or more children 2.1 times higher. Children up to five are in a particularly difficult situation. An extremely worrying fact is malnutrition in families with many children. Another risk category consists of retired people. Level of their poverty increases along with their age advancement.

Education - a good legacy of socialism - reduces the risk of poverty. People with higher education are 2.3 times less subject to poverty risk than the rest. Unfortunately, education has become lately a privilege of well-off families. Average per capita spending on education in poor families is 10.5 times less (!) than in prosperous ones. This is also valid for health-care: in poor families those expenses are 9.7 times less than in well-off families.

As we can see, poverty is many-sided in Moldova. But the country both lacked strategy on poverty reduction in the past and still lacks it. It has been two years now since various committees and projects are working, seminars and meetings are held. Nevertheless, there still is no integral vision of the problem and ways of its solution, which IMF/World Bank missions have noted with regret and left Moldova without seeing any Poverty Reduction Strategy that the Government promised to deliver by March 31.

Two years later...

by Anatol Gudim

On 19 April 2001, the Parliament of Moldova gave its vote of confidence to the Government Activity Programme, and the President approved its composition through his decree. The Prime Minister in his turn announced an intention to implement a plan of emergency measures "*Fulger*" ("*Lightning*") for the first 100 days…

Two years have passed. The Cabinet, in an anticipatory effort, adopted on 3 March 2003 the Decision «On fulfilment of the Government Activity Programme «Revival of Economy – Revival of the Country», the results of the socio-economic development of the country in 2002 and of the urgent measures and tasks taken to enhance effectiveness of the public administration bodies», which reads that «in 2001-2002 high rates of economic growth have been achieved and the living standards have increased significantly». Further on, the paper demonstrates data on growth of the GDP, production and services, low inflation, growth of wages and pensions. It especially mentions that the Cabinet "succeeded in avoiding a default" and expresses particular gratitude to one of agencies – *Fitch Ratings* – for upgrading Moldova's rating as regards long-term financial engagements from *DD* (risk of default) to *B-* and hence slightly improving it. Yet, even the new rating is still below the one Moldova had in the complicated 1998 during the regional (Russian) financial crisis.

Still further on, «at the same time, analysis of the socio-economic situation has revealed certain reserves in functioning of the central and local public administration bodies, as well as a certain delay in execution of the Government Activity Programme». But the only thing mentioned specifically refers to the under-collection of taxes into the state budget.

The Cabinet decided: «1) to take account of the course of carrying out the Government Activity Programme … and the results achieved in 2002, 2) to approve the Action Plan for increasing the effectiveness of the activity of public administration bodies and the Action Plan on execution of the 2003 budget». The former plan includes 55 items and is made up based on proposals of ministries and departments, whereas the latter plan includes 44 items and is the produce of the Ministry of Finance. Controls are to be undertaken on a quarterly basis, by 15th of each next month.

The top priorities (term of execution was due 31 March 2003) as follows: «developing the Strategy of the Public Sector Reform» and «developing the final draft of the Strategy of Economic Growth and Poverty Reduction». The term expired; the controls are over; the paperwork… is still being drafted.

This far from univocal Cabinet paper mirrored the style the Government works: optimism with no long-term priorities, attention to the form and quick reaction with negligence of deeper processes going on in the economic and social spheres.

Administrative and to a large extent populist Government actions have created in 2001-2002 a phantom positive result, which, on the surface, showed in form of GDP growth and higher expenditures for social needs, including those for education and social assistance. Yet, cumulatively the Moldovan economy has been showing signs of imminent danger. They become apparent both through the alarming amount of the state debt, both foreign and domestic, and through the acute shortage of investments, slow process of creating new jobs, mass labour migration of the most active part of the Moldovan able population abroad, the misbalance between the domestic demand and supply (hence the increase in imports), weakening of the role of exports as an engine of economic growth, the increasing trade balance deficit of the country.

It is not only wrong to overlook the existing limitations of economic growth, but potentially dangerous for the future of the country. Of course both the Government and the people are hectic about the 16% GDP growth registered over the past three years. For the sake of the truth, one should bear in mind that value of the Moldovan GDP in 2002 amounting to 22.04 billion MDL (US$1.62 billion) is 19% or one fifth lower the GDP in 1997, while Moldovan exports in 2002 worth US$666 million were US$224 million below the values of exports in 1997. Apart from that, a closer look at the structure of the GDP and its increment reveals that the input of the production sector (industry, agriculture) is rather modest. According to the Ministry of Economics' data, out of the 7.2% GDP growth in 2002, the growth of the added value of the industry and agriculture accounts for 1.6% and 0.9% correspondingly as compared to the 2.6% in services and 2.1% on taxes on goods and imports. As we can see, unfortunately no quality change has occurred in the Moldovan economic growth yet. On the other hand, it is impossible to change the structure of growth over two-three years as it requires structural reforms and more time.

In the meantime, the Government has not resolved on the main thing yet, namely how can the entrepreneurial and investment climate be improved? How can the inertia of the state administration be fought? What our practical steps as a future close neighbour of the enlarging European Union should be?

One has to admit frankly that in 2001-2002 due to well-known reasons (regardless of the pressure from the International Monetary Fund and the World Bank) have not prompted any constructive changes to the economic policy. Laws have been amended, initiatives to enhance the state regulation methods in the production sphere and proposals for social measures to the extent allowed by the limited resources of the state budget have been launched. However, there has been a clear slowing down of utterly important and at times politically difficult structural reforms. Improvement of the business environment failed, as well as overcoming of the distance between banks and the real sector and reducing shadow economy did. In addition, clumsy administration has worsened relations with foreign investors and international financial organizations.

Since the conventional reserves for economic growth in the country have been exhausted, as President V. Voronin also once admitted, it is not necessary to come forward just with optimistic forecasts, but rather to establish the priorities of economic policy and well coordinated practical measures to modernize the Moldovan economy.

To do that one needs political will, stability in the country and in the Government itself. Unfortunately, there remained in its current composition only a small part, only 7 out of 17, of those who were called to the Government two years ago. In a series of ministries and departments the leadership have changed three times over the past twenty-four months. Is the Cabinet a single team indeed?

Moldova's agriculture: crisis or rehabilitation?

by Alexandr Muravschi

Moldova's agriculture has demonstrated certain success during the last two years. After a decade of decline one can observe for the first time growth in agricultural production. It is also important that in 2002 there was growth in the livestock products. With the account of the developing tendencies, the Ministry of Agriculture projects a 10% growth in the agricultural goods production volume in 2003. At the same time, on the initiative of the same Ministry, the Government accepted on March 31 a special Resolution on the situation existing in the agrarian sector of the Republic and the measures to be taken in order to do the 2003 agricultural spring works within optimal time. Mass media reveals more and more materials about a critical if not catastrophic situation in the agrarian sector. This leads to the conclusion that our agriculture has not yet developed any resistance to weather contingencies and the slightest changes of the latter cause considerable positive and negative differences in the production volume. But can this go on forever? Every year Moldova experiences a heavy hail, spring frosts or drought. These phenomena often serve as a justification for the governing bodies in their failures. However, developed countries' experience shows that it is possible to resist nature knowing how to use the agrarian's economic leverage. Can Moldova create such mechanisms?

In order to answer this question, we should shed light on the main factors that have brought about the production growth during the last two years and focus on their further intensification. For the time being, they are not so numerous, which simplifies the analysis. It is true that no serious change has taken place in the policy of the current Government as compared to that of the predecessors. The fiscal policy in agriculture has remained practically unchanged. The subsidies did not grow. No collectivization happened. Only the administrative pressure on economic entities has grown, some export restricting steps have been taken, while the number of the meetings held has increased. Thus, the Resolution mentioned above emphasizes the need for teleconferences, discussions, meetings and so on. But all this has rather a negative than positive impact on the agricultural development.

The growth results from the following factors:

- overall economic growth of Moldova's products major consumers, i.e. Russia, the Ukraine and Romania, which increased the volume of its agricultural export to these countries and consequently resulted in the production growth;

- private sector in agriculture has practically finalized its stage of formation and entered the stage of adaptation to the market conditions. This is the reason for the Republic's quick recovery after the crashing regional financial crisis of 1998-1999;
- performance of the projects created with donors' financial support in order to create market infrastructure in agriculture (farm stores, business cooperatives, machinery and technological centers);
- grown increase of financial resources in agriculture coming both through commercial bank system and through alternative sources (Savings and Credit Associations, Microfinance Alliance, etc.);
- private (privatized and newly created) processing enterprises started more actively creating their own raw materials source and support farmers.

All this means that Moldavian agriculture has overcome its most difficult period and started recovering. However, a lot is still to be done for the success to be strengthened.

First of all, owners should be given the right for choosing the ownership form and type of economic activities. In this context, the growing pressure of authorities on peasants and their leaders aimed at the rehabilitation of the collective sector disguised as creation of production cooperatives is difficult to understand. No other country sets the goal of creation of production organization forms as a matter of paramount importance in its agrarian policy. All types of enterprises appear as a result of owners' interests and aspirations. This is the reason why production cooperatives cannot practically be found in the developed countries' agriculture because in them an owner loses its individuality and a de-facto ownership rights. The production cooperatives that our collectivization advocates are so fond of speaking have nothing in common with farmer cooperatives in the West. The major purpose of the first stage in the agrarian reform was to form a class of owners able to independently take decisions on the ways of their development. This class is coming into being in agriculture and needs to be supported.

Secondly, it is necessary to strengthen the efficiency of the economic mechanisms stimulating agricultural land consolidation and concentration in the hands of the most effective users. For this purpose, it is necessary to maximally simplify the land sale/purchase procedures and adopt a law on lease that would strengthen the lessees' rights. It is necessary to study Hungary's experience on the payment of special compensations to the pensioners having decided to sell their land.

Thirdly, it is necessary to ensure the influx of funds in agriculture. At the same time, it is necessary to take into account that agriculture by itself is not very attractive for investments, which is true not only for Moldova. The major flow of agricultural investments may come only through the processing industry. For this reason, it is necessary to quickly finish privatization of the remaining wineries and tobacco factories including the Chisinau tobacco factory and to ensure full guarantees for the investors' normal work regardless of the political leadership changes.

Fourthly, the Government and the Ministry of Agriculture should specifically focus on improving the export regime. At the same time, the possibilities that Moldova obtained in the context of its joining the WTO should be used to the maximum including settlement of disputes caused by some restrictions imposed by the EU countries.

Fifthly, with the account of Moldova's limited possibilities in the state subsidizing of agriculture, the subsidies should be concentrated in the most perspective directions. The losses caused by hail, downpours, etc. should be compensated mainly from the agricultural production risk insurance system.

Sixthly, the work on the agricultural sector's infrastructure should be continued, i.e. networks of veterinary centers, artificial insemination centers, wholesale markets, agricultural machinery repair and maintenance centers should be created.

The dependence of Moldova's economy on the whims of nature will decrease and the Republic's agriculture will become competitive on the world markets, while the villagers' income will grow only provided that all the measures mentioned above are observed along with the macro-economic stability preserved and other industries of economy and primarily the non-agrarian sector in the rural areas developed.

Raions and economy

by Anatol Gudim

So, local elections are over. And now workaday routine activities begin – practical developing 32 new (old!) raions and debugging their administration. It lies ahead to get back buildings (majority of which are leased out or privatized), fill them with personnel; arrange communications, statistics, etc. A particular problem is employment, which requires measures of supporting entrepreneurship and initiative people. Pre-election political rhetoric is gradually fading and the main thing is being brought to the forefront – what good will return from judetses to raions bring to population and economy, which is – as well known – primary.

Territorial administration is not an easy task. Countries of Europe (that is called “Europe of regions”) accumulated vast experience in this regard – in legislation, division of budgets, using funds for employment promotion, infrastructure reconstruction and environment improvement.

We, who live in the Republic of Moldova, are still to overpass this way. Situation is being aggravated by that since the very beginning and further, over fifty years the republic (MSSR) was guided by the branch-like principle of planning, allocation of resources and administration under multiple (no less than 10 times!) reshaping of its administrative and territorial division. After 1991, when omnipotent Gosplan and branch ministries faded, territories still got neither rights nor real economic basis in form of municipal property or sufficient local budget revenues.

Orienting itself at European standards of local self-government, Moldova's Parliament ratified during 1997-1998 the European chart of local self-government and through introduction of judetses consolidated the country's administrative and territorial division. It was hoped that there would be benefits from potential of larger regions. Later on, though followed changes rather formal than essential. Besides, due to sharp expansion of state apparatus of the higher, national level, it has also happened at the local one.

Despite transition to the market economy, local authorities did not find any specific stimuli for entrepreneurship development (except for personal participation). Indicators of this drama areas follows: 68% of enterprises and 57% of financial assets turnover of SME are registered in the Chisinau municipality – closer to the Parliament and Government, tax and customs departments, licensing chamber, etc.

What is to wait for now, given the return to raions? The Government recalling its promise to cut down expenditures approved on June 10, 2003 structure and personnel of raion, municipality and community administrations so far. At that, as the Prime-Minister said "in order to increase their efficiency we will also resort to dismissal, but it will be done under the legislation". Let us hope that more essential changes in rights and functions of local administration will follow, first of all as regards local socio-economic development.

Otherwise we will not avoid another wave of "consolidation-fragmentation", as it has already happened in the past. Indeed, history teaches that it teaches us nothing:

- May 1948: the second session of the Supreme Soviet of the MSSR abolished judetses and established 60 raions on the republic's territory;
- The 50s: number of raions decreased, at first down to 46 (1950) and later – to 35 (1959). At the same time, it was considered expedient to unite raions into 4 circuits (Baltsi, Chisinau, Tiraspol and Cahul). By the way, the present building of the Academy of Sciences of the Republic of Moldova was meant for the circuit administration;
- 1963: instead of large circuits, though, at the time of permanent reorganizations of N. Khrushchev there took place abrupt consolidation of raions and decrease of their number to 18;
- but, in the next year already a new wave of fragmentation followed: 1964 – 26, 1996 – 31, 1972 33 and 40 raions in the 80s;
- 1990: Supreme Soviet of the SSR of Moldova, based on Declaration of sovereignty, approved Statute on improvement of the country's administrative and territorial division and charged the Committee on issues of local self-government "present proposals" starting from necessity to have territorial units (judetses, traditional for Bessarabia) with capacious demographic potential and capable financial and economic basis; the Planning research institute substantiated to the Government four variants: 7, 9, 12 or 18 judetses (and seven years later one of them served as the basis);
- 1998: restoration of judetses (10 units), plus ATU Gagauzia; Transnistria has kept 5 raions;
- 2003: return to raions (32), plus ATU Gagauzia (3 internal raions) and 5 raions in Transnistria.

- In soviet times, postulate on “unity of political and economic raion administration, which is a junction point where directives of the party and Soviet power are executed” (CPSU in resolutions and decisions of congresses and conferences, volume 4, p. 234) served as an ideological consecration of “consolidations-fragmentations. When raions were consolidated, it was meant to “cut down state apparatus expenditures” and when they were fragmented – “to bring authority closer to the people”. During 2001-2002 the authorities while substantiating refusal from judetses and return to more fragmented raions produced both (!) these arguments!

It is desirable that it will be that way. But it can be only achieved through refusal from strict centralization and administration, while developing municipalities and raions as self-governing economic communities, susceptible to entrepreneurial initiative and social innovations.

Small potential of each of 40 new/old raions (including Transnistria and Gagauzia) can be compensated – ad exemplum of Poland, Czech Republic, Romania and Bulgaria – through exarticulation of 4-5 “*regions of development*” (North, Center, Southeast, South and Chisinau municipality) on the country’s territory, which economic peculiarities, transport benefits, demographic and industrial potential would allow realization – within the concrete strategy for each programmed region – of large projects of national importance, including with attraction of credits, investments and technical aid both from the CIS countries and European Union.

Stable – for the nearest 10-15 years – combination of economic and administrative division into raions of the country can let us avoid new forcible decisions on number, composition and boundaries of raions, and functions of local development administration will gain a real economic basis and specific social environment.

The customs' stamps drama. Second act.

by Galina Selari

It seems that intensity in relations between Chisinau and Tiraspol has become stronger once more, and again because of the export – import transactions control. It is understandable, if we take into consideration the extreme dependence of small open economy of Transnistria (the same as Moldova’s one) on external trade. Since the middle of 90-s, as it is well known, the external trade of TMR was realized under the “cover” of customs stamps of the Republic of Moldova, resulted in USD 817.7 million external trade turnover in 2000 or per capita 3 time higher as compared to Moldova.

The Republic of Moldova introduced new customs procedures and revoked stamps after its joining to the WTO (May 2001), consequences of these for Transnistrian economy were extremely unfavorable, including reducing exports by 36% and import by 17% in 2002. The

Transnistrian Administration has considered this fact as “an economic blockage” which resulted, according to their own estimations, in USD 170 million losses.

The idea of a federative state proposed by OSCE so unexpectedly at the end of 2002 was backed up by both parties and raised new hopes, including those for economic cooperation as well. The advantages of joint appearance at world markets, investors attracting, and participation in regional projects for South-East Europe were absolutely evident.

Mr. Vladimir Voronin, initiating the elaboration of the new Constitution of the Republic of Moldova (February 2003) pointed out that “the people of Moldovan won’t be able to improve their life drastically only until two armies, two customs and two banking systems exist”.

And now the situation has become aggravated anew. The ground was the Moldovan-Ukrainian Protocol on May 15, 2003 according to which goods can be transported through the customs points on the Ukrainian-Moldovan border including Transnistrian only on the basis of the waybills, commercial and customs documents of the official Chisinau. The last action was followed by invitation to registration of Transnistrian enterprises in State Registration Chamber and receiving certificates of origin in the Chamber of Commerce and Industry of the Republic of Moldova.

Mr. Igor Smirnov in his Appeal to the people of Transnistria (June 30, 2003) considered these as “new cases of blockage of external economic activities of Transnistrian enterprises”. He also mentioned that “categorical requirement to register our enterprises is related with Moldovan official’s desire to control privatization process. And in the near future they will ask for payments of all taxes to Moldovan budget, in order to bereave the Transnistrian population of its economic basis”.

Leaving policy aside, we will try to clarify these two violently discoursed problems, namely providing Transnistrian goods and cargoes intended for export with Moldovan customs stamps and validity of privatization processes in TMR.

Creation of customs points on Ukrainian-Moldovan border. Both for Moldova and Ukraine as future EU neighbors economical practicability of operational customs border is evident because it leads to cutback of “shadow” export-import flows, suspension of smuggling, illegal migration, etc.

In May 2001 the Protocol on Harmonization of Tax and Customs Legislation was already signed by Moldova and Transnistria, according to which the regulation of export-import transactions is based on “tax and customs legislation considering both requirements of World Trade Organization and World Customs Organization and CIS and European countries legislation”[1]. The joint customs control on Ukrainian-Moldovan border should be established beginning September1, 2001.[2]

Moldovan tax and customs legislation in force, in the whole, corresponds with the international requirements and norms, and this fact is recognized by the Transnistrian Administration. Therefore the use of Moldovan legislation requirements for issuing customs documentation fully satisfies the Protocol's provisions. The decision of the question was delayed for two years, but even now the Transnistrian authorities consider the joint customs points as "economic blockage" on the side of Moldova. But why only on the side of Moldova, why not on the side of both Moldova and Ukraine?

The negative attitude of the Administration of TMR to the regulation of customs rules for all economic agents could be explained by the lack of credit to the official Chisinau in terms of the letter's unwillingness to consistently carry out its obligations. We can mention that the Moscow Memorandum on the Basis for Normalization of Relations between the Republic of Moldova and Transnistria states that Transnistria has the right to independently establish and maintain international contacts in the fields of economy, science and technology, and culture, and thus is considered an independent economic agent. The offered temporary registration in Moldova of economic agents from the eastern region and maintenance of their ties with the budget of TMR are far from guaranteeing that this system of relationships with regional budget will be kept after the permanent registration (January 1, 2004).

Constructive solution of inter-budget relations problem by the parties, assumption of the related mutual obligations and, what is the most important, their efficient fulfillment could create a basis for the solution of other important economic problems, such as unification of requirements of enterprises registration, avoidance of double income taxation, and some others. Under such approach the creation and management of the common register of economic agents would turn from the "stumbling block" into the "corner stone" of a single economic system. So far the parties have preferred to use the *language of statements and declarations*

A few words on the legitimacy of the privatization of enterprises. Transnistria demanded (July 3, 2003) that Moldova recognize privatization in the region legitimate as a condition for its further participation in the joint Constitutional Commission. Therefore an Act on Ownership is to be signed, "which will legally guarantee the absence of pretensions of Chisinau to Transnistrian ownership".

Let us turn to the existing agreements. The Protocol on Guarantees for Attraction and Protection of Foreign Investments and Cooperation in the Field of Investments Activity says, "the activity of foreign investors and entrepreneurs on the territory of Transnistria is guaranteed by the laws of the Republic of Moldova, Transnistria and international laws".[3] By this, as we can see, the right of the Transnistrian Administration to carry out privatization basing on their own legislation in force is recognized. It is especially important that the Protocol stipulates the elaboration of the joint project of investment strategy, but actual work on realization of such a vital for both parties decision has not yet been started. What a pity!

Today official Chisinau supports legal (?) privatization, at the same time speaking about probable consequences for the investors who have already privatized some property in Transnistria the Prime-Minister of Moldova doesn't exclude that some problems may arise if the buyers had not consulted the Moldovan authorities beforehand.[4] What is not quit clear here is what kind of investors may face with the problems: local (from Transnistria) and/ or foreign ones. And what about the guarantees mentioned in the bilateral Protocol?

Duplicity and inconsistency of official Chisinau’s statements on such an important question can do nothing but alarm not only Tiraspol but also potential investors intending to realize their projects on both banks of the Dniester.

It should be mentioned that “TirPa”, the first enterprise with foreign (Italian) capital was registered in Transnistria as far back as 1988. Besides, «Itera International Eenergy Group L.L.G.» registered in the State of New-Jersey (USA) is a co owner of the Moldavian Steel Works in Ribnita (MMZ) the main financial donor to the region. Moreover, this company is interested in investment projects in Moldova as well. The latest example is the privatization of “Buket Moldavii” winery in Dubosari. On the request of the Ministry of Economy of Transnistria the pre-sale assessment was done by an audit company from Chisinau. The tender was won by “Aroma” Trade House, a Russian investor that already owns some companies in Moldova.

Common sense and economic interest as we see, have already lead to the bilateral agreements mutual realization of which opens the horizons of creative development as opposed to economic confrontation.

The time calls for the negotiation, not for exchange of declarations in “strong language”. No political compromise can be reached without agreement in the field of economy. That is why now, since it hasn’t been done before, specialists in the different fields of law and economy should joint their efforts aiming at approximation of tax, banking and trade legislation, standards, social security system. We have to go this complex way and it will be shorter if we go towards each other.

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[1] Protocol on Harmonization of Tax and Customs Legislation, 16.05.2001, Tiraspol
[2] Protocol on Harmonization of Tax and Customs Legislation, 16.05.2001, Tiraspol
[3] Protocol on Guarantees for Attraction and Protection of Foreign Investments and Cooperation in the Field of Investments Activity, 16.05.2001, Tiraspol
[4] There are no reasons for confrontation, Nezavisimaia Moldova, 02.07.2003

Export promotion: on paper

by Anatol Gudim

Under IMF's trade restrictions classification scheme Moldova’s regime is rated “1” – the most liberal category. This is what is called “*trade on paper*”. But in Moldova there is also “*trade in practice*” that state hampers through its ministries, departments and agencies creating multiple barriers and traps – officially and unofficially in order to feed the corruption. And this has to be fought somehow. And the Government does that… on paper.

Recently, a grateful domestic producer discovered the following document in the "Monitorul Oficial al Republicii Moldova", #141-145 of July 11, 2003:

Dsposition #72-d, July 7, 2003

Achieving sustainable economic growth depends on the existence of a business environment that ensures that no informal barriers to the exporting economic agents exist. In order to achieve this objective as well as with a view to the most efficient implementation of the Government Decision No. 478, as of April 22, 2003 „As regards the exclusion of barriers to exports" all Ministries, Departments and Agencies will do their utmost to facilitate exports and ensure all necessary support to exporting economic agents. The above-mentioned institutions and their employees will use as guideline in their activity the fact that the decision whether or not to export, at what price, through which marketing channels, and whether or not to use the Commodity Exchange to purchase the goods to be exported, is entirely up to each economic agent.

Prime-Minister of the Republic of Moldova

This masterpiece of the State Chancellery shows that even after 12 years of transition to market economy, when more than 85% of GDP is formed by the private sector, not all employees of ministries, departments and agencies realize that "decision on export, price and its method" does not belong to them, but to economic units! What did the previous decision of the Government stipulate in this regard? Quote:

Government decision #478, April 22, 2003

On elimination of obstacles to export of commodities

With a view to achieve sustainable economic growth, facilitate export of domestic products through creation of favorable conditions for economic units, eliminate all technical obstacles to export, as well as to introduce some new restrictions of this kind, the Government decides:

1. Ministries and departments are prohibited to set any restrictions through departmental normative acts, inquiry of additional documents, besides those determined by normative acts regulating external trade, and establishment of indicative prices for export and other actions making export activity of domestic economic units more difficult.
2. Central public administration bodies are to:
   - revise departmental normative acts to bring them into accordance with requirements of the first paragraph of this decision and inform the Government about the actions made in 30 days;
   - publish internal normative acts in the Monitorul Oficial imperatively that affect negatively or regulate external trade regime, after preliminary coordination with the Ministry of Justice.
3. Ministry of Economy is entrusted with control over execution of the given decision.

Prime-Minister of the Republic of Moldova

So, the Government issued two decisions (identical by implication) on the same problem – overcoming bureaucratic barriers to export. These decisions, unfortunately, are not executed at all. Let us remember that not long ago, the Government approved Strategy for export promotion in 2002-2005 (Decision of the Government #80 of January 29, 2002). Its goal was to "*enliven export and increase confidence of exporters to the policy of the state*".
And even still earlier (April 2001), there was Programme of the Government that stated emotionally and clearly that export is the Moldovan economy's driving force, the main source of budget incomes providing for payment under external debt and so on. However, all this exists only on paper…

The realities are that despite export has been growing over the last three years, its volume in 2002 was only 666 mil USD – still 25.2% less than in 1997, and trade balance deficit (import exceeding export) accounted for 414,2 mil USD. Structure and geography of our export have been changing slowly. Agriculture, food processing and textile products account for more than a half of the total export. Traditionally, due to the bilateral free trade agreement, Russia and other CIS countries remain to be main importers of Moldovan products.

Despite better terms of trade with the EU (in comparison to those with the CIS) Moldova's turnover with this region is still modest. Thus, if share of the EU and CEE in Moldovan export was 21.2% in 1997, in 2002 it accounted for 37.8%; as regards import – 38.6% and 49.5% respectively. Growth of import to Moldova of European goods is preconditioned by the consumption growth. Return growth of export, though, is hindered by both low competitiveness of the Moldovan industry and large food and textile components of Moldovan export, which come up against the EU protectionism in these sectors.

Obstacles that state bureaucracy creates to export are multiple and diverse. In opinion of Ion Mushuc, the president of the "Timpul" business club, "image of entrepreneurs as enemies is being propagated in the society and, as a result, business activity decreases, business retreats into the shadow, many entrepreneurs begin to fear for the future of their business and the country". The "Timpul" club came out on July 15 of this year with an appeal to the President V. Voronin: entrepreneurs suggest the President to express his own attitude towards arbitrariness of the bureaucracy to legal business, create a permanent committee for protection of entrepreneurship within the Parliament, amend the Law on the Center for Fighting Economic Crimes hence bringing it into accordance with the Constitution of the country and international legal norms.

It was July as well when the IMF resident representative, Edgardo Ruggiero, reminded that the IMF Executive Board will not release external financing to our country unless Moldova cancels export restrictions and restores pre-shipment inspection.

Parliament Assembly of the Council of Europe has been also caring for promotion of our export. The other day, it approved resolution "On economic development of Moldova: plans and perspectives" that recommends the country's leadership to stimulate entrepreneurship, remove all export restrictions, implement informational technologies more widely in customs, tax administration, financial service and develop trade infrastructure – standardization and testing systems, marketing, transport services and communications.

Thus, we are urged to practical actions to promote the export. This applies both to a more active utilization of Moldova's accession to the WTO, Stability Pact and Free Trade Area and elimination of formal and informal trade barriers within the country. As for the Government decisions "on elimination of obstacles to export', such decisions are necessary of course, but they have to be executed in stead of being multiple cloned.

Shadow economy as a driving force

by Ion Olan

Recently, Department of Statistics and Sociology announced that share of shadow economy (SE) in Moldova is 31.6% to GDP, according to the "Measuring unobserved economy" methodology recommended by the Organization for Economic Cooperation and Development (OECD, Paris). Meanwhile, our statistics has been claiming this indicator to be no more than 14-17% right up till the end of the 90s. One third of the economy is "in shadow". Is this a lot or a little? It is normal, if compared to Europe. This is the level of Greece, Italy or Spain. In Scandinavia, Germany and Austria this "shadow" is smaller.

The problem though is that according to the unofficial estimates (based on employment, consumption of electric energy and cement, import of oil products and food, transportation volume) share of informal economy in Moldova is much bigger – about a half of the GDP.

And, involuntarily, it became apparent through the Government Decision "On results of the RM Government report to the Parliament" #894 of July 21, 2003: "problems conditioned by natural disasters, shadow economy, contraband are mentioned as ***top-priority***"[1] (italicized by I.O.).

As regards the level of negative impact upon the state budget, SE is indeed like a natural disaster. But unlike drought or heavy showers it is a handmade phenomenon.

It should be admitted though that at the beginning of the transition period SE played the role of a social shock-absorber and was a source of additional incomes for the population, workplaces, as well as cheap goods. Now, when metastases of semi-legal and criminalized SE and corruption stroke the young state, they create evident barriers to attraction of investments and development of civilized forms of entrepreneurship. SE aggravates property differentiation of the population, exacerbates problem of poverty that the state will not be able to solve (even given high GDP growth rates), if the budget is replenished only by the legal sector of the economy and there is no efficient mechanism of entrepreneurial income redistribution.

SE is many-sided. It originates from imperfection of the legislation, labyrinths of regulatory bureaucracy, clannish business, "transparency" of customs borders and "benevolence" of tax bodies. Its effects are also many-sided: macroeconomic, budget, regional and social.

One can judge on the level of SE based on the contrast between 14% Moldova's GDP growth over the last three years and the difficult situation of the country's budget, which lacks funds not only for investments and education, but for daily social tasks as well.

Anyone can see the main, the most profitable SE goods: oil products, food and alcohol, tobacco products, medicines; while the most "unobserved", unaccounted by the statistics branches are trade (where SE is 60%), constructions and transportation, restaurant business, real estate operations.

Shadow flows of oil products and alcohol are striking. Their increase over the last years is by implication also confirmed by the statistics. Thus, according to the RM energy balance, officially accounted import of liquid fuel to Moldova dropped from 1,5 mil ton of conventional fuel in 1996 down to 577-645 thou ton in the last years; alcohol – from 29,7 mil USD in 1996 to 3,0 mil USD[2].

But with all this going on oil products market capacity of Moldova is currently estimated at 1,0-1,2 mil ton. The main consumer of oil products (gasoline and diesel fuel) is motor transport and real sector machinery. Number of registered motor vehicles in Moldova reached 900 thou units, including 280 thou cars, 15,2 thou buses and minibuses, etc. Meanwhile, statistics states that oil products consumption of motor transport is just a half of the mid-90's indicator (in agriculture it is less than a third)[3].

One of the prerequisites for the shadow overflow of oil products from abroad has formed on the 1st of April, 2003, when TMR lowered excises for gasoline (40 USD per ton) and diesel fuel (20 USD per ton). In the Republic of Moldova these excises are set to 88,9 USD and 37,04 USD per ton respectively. Rare initiatives to curtail the oil products smuggling yield usually no practical result (marking of gasoline with special dyestuffs, creation of mobile tax stations on roads, control at gasoline stations, introduction of sales registers).

SE regional aspect is mostly showing in municipality of Chisinau and "Moldovan-Moldavian trade" with Transnistria. In Chisinau and its suburbs real estate operations, different types of trade, pharmaceuticals and restaurant business are the most profitable and the least controllable. Obtaining construction permissions – town-planning certificates and authorizations – remains the most difficult problem for economic units. It takes up to 170 days and a minimum of 1 thou USD to get all necessary acts for construction or commission of a finished building.

Besides, so called "Transnistrian conflict" became a large-scale business for both parties long ago. Transnistrian import volumes are worth paying attention: in 2002 for instance it exceeded export by 206,2 mil USD or 82.4% to the region's GDP, while this indicator in Moldova accounted only for 24.2%. Statistics records import of specific goods in volumes that exceed the regional needs considerably (oil products, alcohol, cigarettes, sugar, cosmetics, medicines, etc.) and their subsequent re-export, to the Republic of Moldova primarily, whose share within the Transnistria's "export" officially accounts for no less than 25%, while within the import to the region – only 7-8%. Substantial misbalance of Transnistrian external trade and such countries as Ukraine and Byelorussia is also interesting: import in 2001, for example, exceeded export by 7,8 and 5,3 times respectively. Noteworthy is the fact that this excess is a new know-how of the latest time. Earlier, statistics recorded an inverse situation: in 1997, for instance, export of Transnistrian goods to Ukraine was twice as much as import, to Byelorussia – 2,4 times more.

There are different "schemes" of "export" to the Republic of Moldova of goods previously imported to Transnistria or produced there. Most of them take advantage of gaps and "unclear spots" in legal documents of Moldova related to its economic relations with Transnistria. There is also a manifest smuggling which employs both economic agents of Moldova and Transnistria, as well as those of third countries.

How can SE be reduced? Should it be suppressed, fought or legalized? World Bank has recently realized a research in Moldova "State Regulation Costs Assessment" in 13 areas of economic activity regulated by the state, which covered 630 enterprises of different legal forms, sectors and localities[4].

The conclusion is obvious – an efficient government policy is necessary to reduce the SE through:

- Raising efficiency of state bodies and reformation of the state regulation system;
- Stimulation of legal business, support of small and medium entrepreneurship and creation of a favorable regime for this sector;
- Creation of stimuli for legalization of the shadow capitals, strengthening the protection of property and entrepreneurs;
- Forced suppression of the criminal SE, contraband and criminal drug and human traffic especially.

All these actions have to be realized at the background of purposeful and consequent market reforms given the concurrent strengthening of legal and financial state control over the economy. And the main thing is: shadow economy must not be considered a natural disaster!

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[1] Monitorul Oficial al Republicii Moldova, #155-158, 25 iulie 2003, p. 89
[2] Statistical bulletin of the Republic of Moldova – 2002, Department of Statistics and Sociology, 2002, pp. 302-428
[3] Ibidem
[4] Независимая Молдова, №124, 25 июня 2003 г.

Investments are needed

by Galina Selari

The maintenance of sustainable economic growth is declared as a priority by the government. At the same time, it would be rather precipitate to assert that factors of sustainable development are already available in the country. There are too many alarming signs: external debt and problem of fulfillment of debt liabilities, aggravated as a result of "freezing" country's relations with the IMF, scarcity of investments, both internal, and external, evident insufficient growth of new jobs and mass migration abroad of most active part of the able-bodied population. According to the Ministry of Economy it is essential to increase the volume of domestic investments by 15% - 17% and to attract not less than USD 80 - 90 million of external investments to ensure the expected GDP growth rates by 6-7%.

The Investment Strategy of the Republic of Moldova, as it is known, was adopted at the beginning of 2002. It is too early to assess the effectiveness of its implementation, so put attention on current situation. At the beginning of the year 2003 in the Republic of Moldova were registered 2670 entities with foreign capital, from which only about 1.5 thousand or only half reported about their activity. Since the moment of registration the total volume of equity capital of the entities has reached USD 671 million, of which USD 414 million (62%) were allocated by foreign investors from 87 countries. At the same time only 14% of the total number of entities have the equity capital exceeding USD 500 thousand; entities equity capital of which does not exceed USD 10 thousand (70% of all entities) mainly prevail.

In spite of the fact that the absolute values of foreign direct investments in economy has been increasing gradually - according to the National Bank data at the end of 2002 the total volume of foreign direct investments constituted about USD 720 million - Moldova is still among the countries with one of the lowest rate of investments per capita which is USD 31 only.

Let's turn to the independent expert's assessment. The World Investment Report for 2002, prepared by the UN Conference on Trade and Development (UNCTAD) used the share of foreign direct investments in the growth fixed capital formation as one of the indicators of effectiveness of state policy in attracting foreign capital. In general this figure constitutes about 25% for the countries of Central and South Eastern Europe and for Moldova it was more than 40%, so it needs some additional explanations. According to the report authors, this "leading" position reflects in Moldovan case just a very low GDP per capita level and a small size of the internal market.

Other two indicators are used in the UNCTAD Report: Inward FDI Performance Index (the ratio of a country's share in global foreign direct investment flows to its share in global GDP) and Inward FDI Potential Index (based largely on the structural economic factors – the rate of growth of GDP, per capita GDP, share of exports in GDP, telephone lines per 1000 inhabitance, commercial energy use per capita, share of research and development expenditures in gross national income, share of tertiary students in the population and country risk). Use of these indicators allows, on the one hand, to abstract from size of internal market (Inward FDI Performance Index) and, on the other hand, to range countries basing on their potential in the field of attracting foreign direct investments (Inward FDI Potential Index).

According to the Inward FDI Performance Index Moldova is included in the group of countries with high index value (for the period from 1992 to 2001 it permanently was 1.7). It means that the country attracted more foreign direct investments that could be expected on the basis of relative GDP. According to the Inward FDI Potential Index the situation is, unfortunately, different. If for the period 1992 - 1994 the value of the index was 0.285 (46-th place among 140 countries), in 1998-2001 the value of the index considerably decreased and constituted only 0.194 (109-th place for Moldova, respectively).

With regard to the both indicators, Moldova was among "front-runners" countries in 1992 - 1994, but because in 1998-2001 the result of significant declines in the Inward FDI Potential Index, the country is referred to the group of the "above potential economies", which means that in order to attract foreign direct investments to the country further structural economic transformations and development of industrial potential are required. Thus, as the evident reserves for economic growth have been exhausted in Moldova well coordinated practical actions on modernization of the Moldovan economy contrary to formal optimistic forecasts take on special significance. Moldova is a small open economy. Joining the WTO and European or regional structures (Stability Pact for South Eastern Europe, Euro Asian Economic Community etc.) provides not only access to new markets, but also new opportunities in the field of realization of the investment projects, simultaneously increasing the requirements to economic and investment policy. Moldova took on the collective responsibility for creation and development of a favorable investment climate in the region as a whole, having signed within the framework of the Stability Pact the Declaration on Attracting Investment to South Eastern Europe, in July 2002.

Will be the year 2003 a turning-point? Meanwhile, it is necessary to recognize, that the last two years, by virtue of circumstances, have not brought constructive changes in investment policy. There were adjustments to the legislation, initiatives on strengthening methods of government regulation in economy, etc.. However, the implementation of some important though politically complex intentions in the field of structural reforms has been slowed down. No noticeable results in the improvement of investment climate, in the elimination of separation of the banks and the real sector and in the reduction of shadow economy have been attained. Inappropriate management has complicated the relations with foreign investors and international organizations.

The present year, nevertheless, is characterized by livening up of dialogue between authorities and civil society mainly with the representatives of business circles both Moldovan and foreign (January - the Moldovan-Bulgarian economic forum, April - the Moldovan-Russian economic form, June - first session of the Moldovan-American committee on economic and investment cooperation, July - the Moldovan-Israeli businessmen's forum).

In the common opinion of the participants of all these meetings, Moldova has many advantages, which could attract foreign investors: the geo-economic location, which opens the opportunity of export both to CIS countries – the interest of western investors - and to Eastern and Western Europe - interest of eastern investors (Russia and China); well educated (81% of the population in able-bodied age have secondary education, for the countries with low and average level of income this indicator constitutes about 50%), trained and wage competitive labor force; bilinguism; Moldova feels itself comfortable in cultural environment, both in East, and West.

Unfortunately, the effective use of these advantages hasn't been fully realized so far, as the President V. Voronin put it, "these advantages have to be recreated and money has to be invested into them". So, again, there appears a problem with quality of investment climate in Moldova, as the criterion of market reforms maturity, confidence of business circles in steady property, judicial system, etc.

Strange though, the Republic of Moldova, perhaps, is the only CIS country, which does not have the Law on Investment Activity and as a consequence, the state policy in the field of attraction of internal investments is not precisely determined. Probably, this fact explains the low volume of internal investments. It is impossible to consider the sum of Lei 1.5 billion (2002) sufficient for sustainable development of the country's economy. According to the latest data of the Department of Statistics and Sociology in the first half of 2003 investments amounted to Lei 897.8 million (about USD 63 million) even though it is 30% higher as compared with the same period of 2002 it is evidently not enough. According the sources of investments, self-funding (including individuals' resources) constituted 75%, foreign investments – 16% and only 5% was the investments on account of the state budget. It is clear, that foreign investors will not invest in the economy, in which local businessmen refuse to invest.

Drafting of the Law on Investment Activity, which is to even the rights of local investors with those of foreign ones, started in 2001 and the terms of its adoption have not still been determined. However, the country has some regional experience: it is the Law on Investments and Investment Activity in Territorial Autonomous Unit Gagauz-Yeri (2001). In contrast to the Republic of Moldova's Law on Foreign Investments (recognized by the independent foreign experts as one of the best among similar laws of CIS countries), the law of Gagauz-Yeri does not make any difference between foreign and local investors. On the territory of Gagauz-Yeri all investing agents have incentives stipulated by the Moldovan legislation, as well as additional ones according to the local law. Therefore, today, Gagauz-Yeri, in a sense, can be appreciated by potential investors as an oasis in the Moldovan investment environment.

Businessmen, local as well as foreign, wish for a transparent market with predicted rules. They are eager to work to make the Moldovan market one of most favorable in the region. The first words of Mr. M. Lupu in the capacity of new Minister of Economy (august 2003) are concerned the same matter: "We should win back confidence in state economic policy consistency and predictability of both international donors and Moldovan business circles. Without this our main task – attraction of sizeable foreign investments - can't be solved".

The Budget with many unknown variables

by Anatol Gudim

At the beginning of September the Government website, www.moldova.md, published the draft state budget of the Republic of Moldova for 2004. This is a good example of "glasnost". Moreover, since this draft will be presented to the Parliament only in October and then legislators will discuss it, all of us who are now called "civil society" have the opportunity to take part in this process.

At first sight, optimism of the 2004 budget is astounding. The budget is envisaged to entail no deficit. As before, it is notable for its “social orientation” – 38.7% of all expenditures will be directed to social assistance, healthcare, education, science and culture. Besides, 340 mil MDL are envisaged for raising wages of budget workers. There is an intention to reduce the tax burden: income tax is planned to be cut down from 22 to 20%, social fund payments – from 29 to 27%. Agriculture is not forgotten. 30 mil MDL are allotted to form a fund to subsidize agricultural producers.

All this occurs against the background of positive macroeconomic reference points of the next year – 5.0% GDP growth, low inflation of 4.5% and a national currency exchange rate of 15,2 MDL/1 USD.

Where could one get these revenues? Most of them (65.0%) – as before – will be provided by VAT and excises. Non-tax collections are estimated at just 421.5 mil MDL. Unlike in the budgets of European countries land and real estate tax collections are quite paltry – only 4.2%. Moreover, the Ministry of Finance hopes to obtain donor grants (289 mil MDL) and the proceeds from privatization – 304 mil MDL.

Upon examination of the draft one starts feeling an involuntary sympathy with its authors, the Government and, in the end, the country’s life during the next year. It contains too many “unknowns”. The main questionable issues are as follows:

- Will the country enjoy external financial support? Who will give money and how much? How are old debts to be paid? There are 371.9 mil MDL (24.5 mil USD) foreseen for these goals, which is 3 times less than the impending payments;
- How effective for economic activization will tax rate reduction turn out? Will it not destabilize budget revenues?
- Will it be possible to reduce the shadow economy (according to the Department of Statistics, it provides no less than 1/3 GDP), especially in its most significant “strongholds” – alcohol, tobacco, fuel, medicines, real estate and export-import operations?
- What will be possible to privatize? “Moldtelecom”? Northern electric power distribution networks? Wine factories? “Zorile” or “Viorica”? It was not possible this year;
- Do we still have to increase expenditures for maintaining the state apparatus? Shouldn’t we still this year bring into effect Iovv’s plan to reorganize Government structure and functions? After all, the apparatus of some branch ministries “devours” more money per year than enterprises “under their jurisdiction” bring into the state budget! What state apparatus quality are we talking about when only 14 out of 32 new raions have presented draft raion budgets to the Ministry of Finance on term (1st of August)?
- How can wages be raised when wage arrears are already estimated at 176.5 mil MDL (12.7 mil USD) having grown over the last month by 23.9 mil MDL? What are the sources of finance (211.7 mil MDL) for social compensations to some categories of the population (invalids, war veterans, families with many children, etc.)? This year most of these means were provided by the European Commission, USAID and other donors.

Everything indicates that there were difficulties in designing the draft. Its social orientation is due to poverty. Other countries make up “budgets of development”, while we allot only 90 mil MDL for investment (1.7% of expenditures!), 66 mil MDL for scientific research (including 3,2 mil MDL to the Academy of Sciences, which is less than the cost of maintaining some ministries).

The initial variant of the 2004 budget is a child of the Ministry of Finances. The participation of other state bodies, including the Ministry of Economy, was minimal. It is interesting that the Ministry of Finances is found within the state budget structure in the honorable section 1 – „Servicii de stat cu destinație generală” (together with the Parliament, Presidential apparatus and State Chancellery of the Government), while the Ministry of Economy, as a poor relation, follows all branch ministries in the final section 19 – „Alte servicii legate de activitatea economică”.

In the meantime, one would expect the participation of the Ministry of Economy to be decisive during elaboration of the philosophy and main allocations of the budget for 2004. For the sake of the cause the Ministry of Finance that manages the technique of budget design and execution quite well needs a partner and an opponent.

To tell the truth, one should admit that it was the Ministry of Economy that placed itself in such a humiliating position. It was as early as spring when the Ministry (by 31^{st} of March, as coordinated with the IMF and WB) was to finish the work on the Economic Growth and Poverty Reduction Strategy for 2004-2006. In this case, the budget for 2004 would represent an instrument to realize this strategy in the first year and would be linked with the solution of key problems of this mid-term.

Since there is still no Economic Growth and Poverty Reduction Strategy (discussion with civil society is promised in autumn) and the state budget for 2004 was made up autonomously, two paths of development are possible:

1. The Parliament will discuss and approve the budget quickly (and formally), aware of so many “unknowns” that it will inevitably have to introduce multiple amendments during execution of the budget in 2004 (as in 2003);
2. Consideration of the budget will last till the end of the year and it will be already the 2004 Q1 when it will be approved. In this case, one would be able to discuss the realities and unclear positions of the budget with the autumn missions of the IMF, WB and other donors, and perhaps take more determined actions to launch the “second wave” of reforms in the country and the practical participation of the Republic of Moldova in European integration processes.

Naturally, the second variant is more preferable. But its realization requires the united creative work of the Parliament and Government, rather than the Ministry of Finances alone. One thing is clear: we are in for a very difficult year financially.

The paradox is that the country’s threatening budget problems intensify against the background of the sprightly GDP growth rate: +2.1% in 2000, +6.1% in 2001, +7.2% in 2002 and no less than 7-8% in the current year. The forecast for 2004 of both the Government (+5.0%) and external experts (+4-5%) is still optimistic. No one is talking about a default yet. Perhaps in fact, it may pass us by once more and we will experience the viability of the old slogan “There are no such fortresses the Bolsheviks cannot storm” again?

European integration concept - at last…

by Mariana Argint

The Government has finally prepared the draft of the "Conception for European Integration of the Republic of Moldova". Its discussion and more accurate definition are yet to come.

This is a very belated document. And it is also unclear why it is called "conception" instead of "national strategy" as in other countries? Thus, it was November 1993 when President Mircea Snegur sent a letter to the European Commission Chairman Jack Delore proposing to stir up the formation of political and legal grounds for relations between the Republic of Moldova and the European Union (EU). In 1994, the Commission assessed the situation and acknowledged the positive changes in Moldova - the first multiparty parliamentary elections, the new Constitution, liberalization of the economy and financial macro stabilization, and democratization of societal relations.

This was followed by the signature of the Partnership and Cooperation Agreement (PCA) between the EU and Moldova (1994) and its coming into effect (1998), which was an official recognition of Moldova as an EU partner for political dialogue and legal and economic cooperation.

This agreement though, unlike the EU "association agreements" with the Central and Eastern European countries, by no means was a prelude to further accession to the EU. It was rather meant to Europeanise our young state and bring the quality of its state system, economy and social life as close as possible to the Copenhagen criteria of the EU (1993) for new eventual EU members.

Unfortunately, the EU-Moldova agreement has been implemented slowly over 1998-2000, and the fault was mostly ours. As strange as it may seem, despite the new emphases emerging every year in policy and practice of the country's transformation, the agreement has never underwent any adjustments. Both parties - Brussels and Chisinau - admit that the PCA potential has not been used in full measure. Last year, at last, it was decided to concentrate the cooperation in five areas: legal harmonization, customs and cross-border cooperation, fighting criminality, examination of approaches towards interaction of the parties within the Free Trade Area, and investments.

Over the past decade Moldova nonetheless preferred staying within the so called "grey zone", a zone of geopolitical uncertainty. But even in this situation the country has already received aid worth more than 240 million euro from the EU within the framework of TACIS and other programs. In addition, it has been announced that another 50 mil euro will be alotted to Moldova for 2003-2004. These funds are meant for macroeconomic support, social assistance, stimulation of private sector and export, as well as for reformation of the administrative and judiciary systems.
At present, though, Moldova's leadership puts the question more assertively - it has declared that European integration is an external policy priority of the country. According to President Vladimir Voronin (January 2003, during a meeting with the diplomatic corps), "the Moldovan leadership perceives European integration as a three-dimensional process. Firstly, this is a path to reintegration of Moldova itself based on modern legal standards. Secondly, European path means for Moldova modernization of the country's economy based on universally recognized mechanisms functioning in Europe and in the world. Thirdly, European integration means formation and development of our political institutions, reformation of public administration with strict delimitation of functions and powers proper to a democratic state with market economy".

The President expressed himself even in a more clear cut way on Independence Day, 27 August 2003: "the program of Moldova's European integration is the main strategic document for us, which is superior to all party programs and current tasks of all power branches".

These are our intentions. The Government is convinced that there are no fundamental contradictions between the pro-CIS and pro-EU policies. Apparently after the CIS Summit hosted in Yalta on September 18-19, Moldova's belief in CIS was shattered significantly, whereas in the EU, on the contrary, was strengthened.

However, European Commission has a more clear position on this: in the mid-term perspective Moldova has no chances of becoming an EU member. In a more distant future this is not excluded. Possibilities of this will grow as the country connects to the processes of stabilization and association in South East Europe. The EU has recently declared that it was ready to work out a plan in 2004 of priority EU actions for Moldova.

European choice is a strong incentive for Moldova, since it is this choice that provides the country with both democracy and institution-building, internal stability and external security.

Moldova today is a partitioned state located at the periphery of the uniting Europe, whose existence is complicated by the frozen Transdnistrian conflict. Efforts to reunify the country within a "common state" will enable Moldova to use the Transdnistrian issue as a good argument: conflict resolution would not be sustainable unless backed up by perspectives of EU integration, by promises, for Transdnistria as well, to take advantage of the benefits of political and economic association with European Union.

Proposing new and new initiatives along the European direction (as also regards settlement of the Transnistrian conflict), we should not slacken efforts to realize political and economic clauses of the EU-Moldova PCA. What can PCA give to Moldova as regards approaching Europe? This includes:

- Creation of joint bodies (including at the higher level) to examine all problems related to partnership and cooperation between the RM and EU;
- Formation of the "functioning" legal environment through approximation of Moldovan legislation to the EU one;
- Accustoming to universally recognized rules of international trade;
- Gradual transition to normal conditions of competition, which in the end should raise the economy's efficiency;
- Financial assistance of the EU in developing key sectors of our country, which helps implement economic and social reforms.

One of the priority directions of the PCA implementation is the creation of a free trade area between Moldova and EU. It is important to mention that since at present Moldova still cannot assume obligations to create an area of free trade with the EU (due to the underdeveloped competitive environment and administrative capacities), the EU is willing to consider new possibilities of providing Moldovan goods with access to the market within the framework stipulated by the WTO.

Now, the most realistic for Moldova is its participation in processes of sectorial integration with the EU. This means ensuring Moldova with autonomous trade preferences followed by the Free Trade Agreement, infrastructure development, border control etc.

Speaking of Moldova's European vector, one should consider both "pros" and "cons" of such orientation. Indeed, it could be already in the near future when Moldova as a new neighbor of the EU will be able to count on enhanced financial and technical assistance, facilitated visa regime and access to new markets.

At the same time, given Moldova's slowness, some of these advantages may turn into problems.

Thus, for instance, transition of the united Europe to common norms and standards will undoubtedly facilitate movement of goods throughout its market. With this in mind, Moldova should provide "euro-harmonization" of its standards and requirements and the conformity assessment procedures. Sluggishness will sharply worsen the access of Moldovan products to European markets, especially foodstuffs.

Another important aspect is attracting foreign investments into the country. And this requires urgent improvement of the country's investment climate; otherwise, after the EU enlargement, it will be our neighbors - the new EU members - who will become the main recipients of European subsidies and technical assistance programs. It is not excluded it will be the new members' economies that the EU will encourage investments into, leaving the "tardy" Moldova outside this activity.

The process of Moldova's rapprochement with Europe requires a lot of effort and time. Therefore, it is not rare when the question arises: is EU membership an absolute necessity for

Moldova? To answer this question, a more detailed analysis of the impact of EU policies (Common Agricultural Policy, Social and Labor Market policies, Standard and Costs in Environmental Protection etc.) on our national interests is necessary.

According to President Vladimir Voronin, "the enthusiasm of all branches of power is now focused on European integration". But this enthusiasm (!) also requires a wider public support. It is still unstable. According to opinion polls, the population favors EU and CIS almost equally. Taking this into account, the two-level EU policy concerning Moldova is important - at the level of the Government and the civil society. This will be the case when in our country the notion of "integration" will link closer to such notions as "democracy" and "development".

Ultimately, all of us need a democratically stable Moldova, integral from the political, social and territorial points of view. And its approach to Europe will undoubtedly enhance the external positive impact upon the quality of governance, business and living in our country.

Can de-urbanization be stopped?

by Anatol Gudim

The new times have brought considerable changes to the Republic of Moldova. Such changes include openness to the world, macroeconomic stabilization, property reform, rise of the market and private sector, land privatization, trade liberalization (external and internal) and democratization of public life. There are, however, spheres of life where changes have been of a destructive character. Amongst them are expansion of the poverty zone and social inequality, emigration and mass labor migration abroad, the deindustrialization of towns, the collapse of social infrastructure in rural areas and finally the stagnation of ecosystems.

The majority of these negative processes appear locally. Despite this, problems of managing local development got the least attention of all our reforms.

In part, this is an echo of recent past, since branch-like state management dominated during the soviet period and it was central government and branch ministries that disposed of all management instruments and resources. After 1991, ministries (except the Ministry of Finance) were deprived of instruments such as the right to distribute investments, funds, etc., yet local bodies (districts and towns) did not get them instead – either in the form of self-administration functions, or in the form of municipal property or sufficient incomes for local budgets. Instead of the “federalization of the country’s budget” we got quite the opposite – its even higher centralization. The lack of consideration for the local needs is one of the main causes of inefficient reforms in Moldova.

De-urbanization as a fact. The transition in Moldova was marked (among other things) by reduction of urban population. It numbered 1.91 mil persons throughout the whole territory of the country, including Transnistria, as of January 1, 2003 or 45.3 percent of the population. On the right bank of the Nistru river it numbered 1.49 mil, or 41.4 percent of the total population. The main causes are the deindustrialization of towns, stagnation of their infrastructure, and depopulation, which is deeper in towns than in rural areas.

The fastest urbanization of the country, as is well known, occurred during 1960s – 1980s when circa 300 new industrial enterprises were placed on its territory. They used both imported raw materials (in the energy sector, machinery, light and furniture industries) and domestic ones (in the food industry and in the production of construction materials). As a result, the urban population grew from 670 mil persons to 2,1 mil persons over the 60-90's that is, threefold! The urban skeleton of the country was formed of 21 towns (a large one – Chisinau, three medium ones – Balti, Tiraspol and Bender; the rest are small towns with populations of no more than fifty thousand people) and 45 urban villages.

After 1990, under the complex crisis of the economy, the urban population dropped by 154,4 thou persons, the figure equal to the number of people living in Orhei, Soroca, Ungheni and Cahul taken together and exceeding the current population of Balti, whose population in turn has reduced by approximately 10.0 percent.

Urban population dynamics (including Transnistria)

	1960	*1970*	*1980*	*1990*	*2002*
Thou pers	670,1	1130,1	1586,5	2069,3	1914,9
Percent	23.0	32.2	40.1	47.4	45.3

The crisis of cities has mostly affected small towns and new urban villages, especially those based on a single enterprise: Rezina (a cement factory), Cantemir (a tinned food factory), Briceni, Alexandreni, Glodeni (sugar refineries), etc. Chisinau turned out to be relatively stable. Its population (within comparable boundaries) reduced slightly: from 661,4 thou persons according to the 1989 census to 660,7 thou persons as of the beginning of 2003. But it has been the municipality of Chisinau where the most part of business of the country has been concentrated: 68 percent of all small and medium enterprises, 75 percent of their output and 57 percent of the employed.

Among Moldovan citizens going abroad 35-38 percent in the last few years have been urban residents (according to the Department of Statistics and Sociology). In the Q2 2003, for instance, there were 88,3 thou of them, which is equal to the population of ten(!) towns like Cantemir.

Moldova is manifestly starting to look more rural. This occurs against a background of a rather urbanized structure of its neighbors – Romania and Ukraine, where urban population accounts for 55% and 68% correspondingly. The only European country where urban population is smaller than the Moldovan one is Albania.

Will the 2003 administrative-territorial reform provide for a revival of towns? Most likely, the answer to this question will be negative. The return to 40 territorial raions (32 on the right bank of the Nistru, 3 in Gagauzia and 5 in Transnistria), most of which have small demographic and production potential, might "bring the authority closer to the people", but it surely will not allow the concentration of resources – either from the state budget, or from the outside. All cities (except Chisinau and Balti) and districts will remain doomed for a long time to depend on transfers allotted by the Government. It is indicative how the Government (Decree #93-r of September 8, 2003) plans to hold its field sessions in Straseni (September), Ocnita (October), Basarabeasca (November) and Stefan-Voda (December). These sessions are intended to examine issues that are quite topical for these towns and districts: such as entrepreneurship development, provision of the population with natural gas, electric power, drinkable water and so on. Among those mentioned as being "responsible for the preparation of these sessions" were the Ministry of Economy, Ministry of Agriculture and Food Industry, Ministry of Ecology and Constructions and a series of departments. But no local bodies were mentioned. Besides, towns are now "built-in" into raions: all interrelations between the towns and the state budget (including transfers) are carried out through the raion financial services.

Such an attitude towards towns cannot be considered as productive. Moreover, ever since the 14th century the authorities ruling over Moldova divided the country in different ways (such as tsinuts, rayas, judets, raions), but the country's "skeleton" has always been "cemented" by cities and roads. Now, taking account both of the current general distress and of future tasks, one should admit that it is not realistic both to raise and equalize development throughout the country's territory concurrently. It is necessary to mark out peculiar "growth poles".

Towns as poles of local growth. World history gives many examples of the stimulating and organizing role of cities in the development of regions and countries, for example, the city-states of ancient Greece, Hanseatic cities of medieval Germany, the towns-colonies of the Black Sea, etc. Towns played a particular role, especially during crises, in Moldovan history as well.

Taking this into account, *the concept of nodal or polarized districts* formed around cities as the nuclei of administrative, economic and social activities is universally recognized in regional theory and practice. The functional interconnections in such districts occur most effectively through flows of labor, resources, goods and services and transport ties. Towns as growth poles of such regions determine the development character of territories, which are drawn towards them, and concentrate such spheres as entrepreneurship, "business for business", investments, financial operations and education.

The regional policy realized during the 1970s – 1980s in the MSSR (besides elements of voluntarism) in the scientific respect was based on distinguishing homogenous regions (zones of agricultural specialization), nodal regions (towns – industrial parks, promising settlements), as well as programmed regions (such as programs for developing Chisinau or the South of the country).

The principal long-term documents were the "Multilevel regional planning of the MSSR" and "MSSR regional settlement system". In correspondence with these plans the country was demarcated by *4 group settlement systems* (North, Center, Southeast and South) and *8 planned zones* (their centers were Edintets, Balti, Ribnita, Ungheni, Chisinau, Tiraspol-Tighina, Comrat and Cahul), which – in their turn – were divided into *36 subzones and 86 microzones*.

Depending on the complexity of their functions towns were divided into 4 levels: *multifunctional centers of group settlement systems*; *interdistrict centers*, whose influence extends to several low-level districts; towns – *centers of low-level districts*; *local centers*.

During the last decade, the scientific and project basis of regional policy in the Republic of Moldova was not modernized and the situation at the local level became worse everywhere and to virtually equal degree.

That is why the Government's possible initiative (developed by the Ministry of Economy or the Ministry of Ecology, Constructions and Local Development?) for sustainability and realizing the concept "Towns as Growth Poles" could base itself (just for a start!) upon its "predecessors" – the research output of the "NII planirovania", "KievNIIgiprograd", "Moldgiprostroy" (now "Urbanproiect") and "Moldgiproselstroy" (now "Ruralproiect"): the "Multilevel regional planning of the MSSR", "MSSR regional settlement system", and "Methods and variants to form the network of administrative-territorial districts" approved in its time by the Government and still in operation owing to the lack of new elaborations.

Based on the aforementioned there are 12 towns that might serve as possible "growth poles" – for economic, social and cultural activization of the surrounding territories: Balti, Edinet, Soroca in the Northern region, Chisinau, Orhei and Ungheni in the Central one, Comrat, Cahul and Taraclia in the Southern one, and Tiraspol, Ribnita and Dubasari in the Southeastern region of the country.

Focusing the attention of the Government on a limited circle of cities will allow saving time and resources. Such an approach will surely provoke objections both of the administrations of other towns and raions, and their lobbyists in the Parliament and the Government. In this case however, we will once more miss the opportunities that marking out priorities in economic policy could bring. We have already made the mistake at the dawn of reforms of not choosing priorities of both manufacturing industry and agro-industrial complex, and we are trying to rectify it now.

The practical implementation of the concept "Towns as Growth Poles" presupposes the formation of its legal basis, trustworthy statistics on towns and raions, and a mechanism for financial interrelations between the center and those key towns. This is not an easy work, but it is a concrete one, and so it can become quite a constructive part of the Economic Growth and Poverty Reduction Strategy (PRSP) that the Government is formulating now as its economic policy main document for the next few years.

Moldova – Transnistria: Clash of Economic Interests

by Galina Selari

Moldova and Transnistria agreed on the “common state” formula and 5 common spaces – legal, economic, customs, defence and cultural as far back as 1999. Further steps seemed a mere technical matter – documents’ development.

But it turned out to be quite different from what was expected. Withdrawal of rights to use customs stamps of the Republic of Moldova from Transnistria “materialised” in the notion of “economic blockade”. Gradually increasing tension has been becoming stronger and stronger during 2003, in spite of the fact that the parties have, as before, agreed that reintegration is the single opportunity both for conflict settlement and ensuring of economic revival of the two sub-regions. To achieve this goal the elaboration of the Constitution of the united state has been started. Nevertheless, the nerve-strain can be compared to some extent with the situation that preceded the 1992 confrontation, but *now, however, the proscenium is taken not by immaterial problems – language and history - but by economic interests focusing on whom the property belongs to and who will control the financial flows.* That’s why the current aggravation of the situation represents no less danger than that that occurred in early 90s.

Insisting on their own rights the parties seem to compete with each other in pilling up restrictions for the economic agents and population of the far bank. And this is happening notwithstanding the fact that as early as 1992 after the “heated” phase of the conflict it was agreed that “conflicting parties considered application of any sanctions or blockades inadmissible. In this context any barriers to free movement of goods, services and persons shall be eliminated”.

Practices used during last months by both parties in order to ensure these economic freedoms have given rise to surprise. Let us bring them back to the mind:

First act: spring – summer 2003

- May 15, 2003 – the Customs Department of the Republic of Moldova and the State Customs Service of Ukraine signed the Protocol on Mutual Recognition of Motor Waybills, Commercial and Customs Documents and, as a result, starting from May 25, 2003 the entrance of goods with Transnistrian customs documents to Ukrainian territory was ceased;
- June 12, 2003 – the Government of the Republic of Moldova introduced temporary (till January 1, 2004) registration of Transnistrian economic entities in corresponding Moldovan institutions.
  The Administration of Transnistria considered these as toughening of “economic blockade” and Chisinau’s pretensions to the sub-region’s property and took retaliatory as well as prohibitive, measures;

- July 1, 2003 – gas supply to the villages Malovata and Cocieri which are under the Republic of Moldova's jurisdiction but are situated on the left bank of the Dniester was suspended on the grounds of arrears.
- July 14, 2003 – the Decree of I. Smirnov introduced a special customs duty at the rate of 100% of goods customs value for all commodities imported from the Republic of Moldova ;
- July 18, 2003 – the Decree on Establishment of Most Favourite Nation Treatment in Trade and Economic Relations with Ukraine was issued.

Further, an utterly absurd situation based on reciprocal accusations of "jamming" has arisen and resulted, since the middle of September 2003, in the breakdown of telephone communications between Moldova and Transnistria causing considerable damage to the economic entities and population. Can we believe it is taking place in Europe?!

Second Act – autumn 2003

- October 15, 2003 – the Government of the RM took the Decision to establish stationary customs posts in order to apply the customs control rules to goods brought from Transnistria;
- November 4, 2003 - the Transnistrian party suspended its participation in the sittings of the Joint Control Commissions.

All these actions on "isolation" and "forcing to harmony", etc. resulted in sizeable decrease in reciprocal trade between the sub-regions, the shift of economic entities from both sides of the Dniester to shadow economy and, as the consequence, activization of contraband and corruption. A seemingly unexpected surge of contradictions against the negotiation background arose to a considerable degree out of the fact that *for the first time after 1992 the economic interests of so called elites – the old one and the new one – and certain "business groups" from both sides of the Dniester had been visibly damaged.*

As the secret came to light, revealing the domination of economic interests, it is time to liven the search for "common grounds" primarily in the field of economy. The problems which both Moldova and Transnistria are facing with are similar. And it will be logical to seek for the possible ways of their settlement together.

The increase of the level of living standards and maintenance of sustainable economic growth are strategic goals for the both sub-regions. Reviving of real sector both in Moldova and Transnistria has been advancing slowly, thus the need of "second wave" of reforms both in industry and agriculture and social policy has come to a head. Moreover, both parties are facing with tough budget constrains associated with the necessity to maintain a social safety net while at the same time the burden of taxation needs to be reduced to encourage entrepreneurship and attract foreign investment.

The situation is getting even more complicated if we take into consideration that for both Moldova and Transnistria the problem of external debt servicing is very acute and as a consequence brings about “twin deficit” in the budget and balance of payments. The problems like these are typical for many economies in transition but it could be easier to solve such problems within the frame of “common state”, involved in the stabilisation and reconstruction processes in South – East Europe.

As time goes on the external factors can further contribute to a balanced and, what is most important, civilised conflict settlement. First of all it is related to the European Union enlargement to the East and surely to the new Neighbourhood Policy of the EU. If the Republic of Moldova will be the first-hand EU “neighbour” not earlier than 2007, Russia, Byelorussia and Ukraine will be neighbouring the EU as early as 2004.

And what is more, now the concept of “common European economic area” is far more exceeding the frames of enlarged EU. It is mainly related with transformations of Russia’s and Ukraine’s relationships with European countries, strengthening and intensification of economic partnership. It is evident that such partnership will become stronger following theirs accession to the WTO and implementation of the Agreement on Common Economic Area signed by 4 largest CIS countries – Russia, Ukraine, Byelorussia and Kazakhstan – in September 2003. The fact that the same countries are both key and common trade partners for the two sub-regions of Moldova will undoubtedly affect relations between these countries and the “common state” and at the same time between the sub-regions.

The “political and economic” tension between Moldova and Transnistria aggravated during the spring – autumn 2003 has negatively affected their reciprocal trade. According to the Transnistrian Republican Bank data the share of the Republic of Moldova in total Transnistrian external trade has reduced to 9% (the lowest indicator over the last years). It is interesting that the *most sizeable decrease was registered in Moldova’s inflows to Transnistria* but at the same time the opposite flows of goods *to* Moldova even increased by 24%. And Transnistrian export growth to Russia and Ukraine amounted to 300 and 84%% correspondingly. It is also interesting, that according to the social and economic forecast of Transnistria for 2004 Russia and Moldova will *remain* the main Transnistrian trade partners within CIS (38.5% of total external trade turnover). And this is observed under circumstances in which the favourable conditions were created for Ukraine – products imported from this country are not subject to customs duties, excisable goods being the only exception but Moldova’s ones are subject to special 100% duty.

A way out of the current situation which considerably damages both Moldova’s and Transnistria’s economies can be found solely by means of a mutual compromise including that on economic problems solutions. It seems that this compromise should be realised during the initial stage of transition period of reintegration and this point was set up in the draft agreement on settlement proposed by OSCE (July 2002, Kiev) but has never been realised.

The attempts to de-block economic “obstructions” through official negotiation process have been to no effect for the time being. So, involvement of entrepreneurs and non-governmental organisations in discussions of economic aspects of Moldova – Transnistria relations would be in favour. These aspects are much spoken of: property, privatisation, financial flows, customs procedures, registration and taxation, free movement of persons.

Why not to discuss the possibility for the parties to sign the document in which it will be stated that until the Constitution of "common state" is approved:

- respectful attitude to the property in the territory of the both sub-regions based on mutual guarantees of efficient use and management of the property with consideration of each parties interests and interests of the future "common state" will be guaranteed;
- economies of the two sub-regions will operate during the transition period within the framework of existing legal environments namely those of the Republic of Moldova and Transnistria.

It is understandable that these suggestions are to be discussed. But theirs acceptance could in many respects defuse the current situation, mutually undermining and often absurd.

2003: We managed to hold out, but failed to break through

by Anatol Gudim

The Government thinks "2003 will go down in history as a year of new achievements in socio-economic development of the Republic of Moldova" (V. Tarlev's speech in the Parliament, 26.12.2003). But Fitch Ratings, an international agency that the Government respects (London/New York), evaluated, nonetheless, 2003 as "another disappointing year for Moldova. The government has failed to accelerate structural reforms" (5.12.2003).

The truth apparently is somewhere in between. One could assess work of the Government, Ministry of Finance and National Bank as successful based on the fact that they managed to maintain macroeconomic stability, there were positive changes in industry, constructions and services, incomes of the population increased, but the Government's activity along the reformation path has been mostly based on the "one step forward – two steps back" principle, which was the cause IMF and World Bank were so evidently disappointed saying that *Moldova's liberal-market economic course is being transformed into state dirigisme*.

PR-economy

Any government has to produce optimism. And ours does the same. Results of the year, according to official estimates, are very optimistic: GDP grew by 6.8%, industry – 17.0%, domestic investments – 23.0%, export – 25.1%. State budget incomes increased by 36.2% and incomes of the population – 19%, including average monthly wage in the national economy – by 31% and pensions – by 28%. Social sphere received 53.7% of the total expenditures of the consolidated budget.

These indicators of "achievements" were published many times to confirm that actions to revive the economy were correct. It would be proper, though, at the same time to mention the risk factors as well that in 2003 intensified, rather than subside. Among them are:

- *Quality, structure of the GDP growth*. Share of real sector is rather small within the 2003 GDP growth (industry, for instance, accounted for only 11.5%). Its largest part is being formed in services, import operations, by means of banking credits, etc. GDP growth given such its structure is not equivalent increase of real resources at all. Especially since the budget has nothing to do with formation and distribution of GDP. Hence the population does not really feel this growth;
- *Unsatisfactory state of business environment,* which shows through insufficient volume and structure of export (it is still less than the 1997 level), uncertainty of foreign investors' disposition, freezing of privatization and preservation of a vast shadow economy sector;
- *Critical state of the country's balance of payment* due to almost double (!) exceeding of import over export, while after relations with IMF and World Bank had cooled off possibilities of receipt of currency through external loans and investments have sharply dropped. Of a little help is replenishment of the country with money transfers of our citizens working abroad – circa 500 mil USD in 2003;
- *Inflation leap* up to 15.7% in 2003 (4.4% in 2002) and 20.0% increase in prices for foodstuff. Approximate 1/3 increase of wages and pensions also left its traces, even though wage arrears reached 175,7 mil MDL (13,3 mil USD). Danger of a critical gap between the need to expand monetary aggregates and capacities of the inflation-free emission;
- *Further increase of external* (1,4 bil USD) *and internal* (2,9 bil MDL) state debt;
- *Unreformed state machinery*, which is the cause many "2003 initiatives" either were not realized, or yielded small or negative results. Among them are: advancement along the way of European integration, implementation of the strategy of economic growth and poverty reduction, development of a competitive environment and small and medium business support, activization of export and foreign investments attraction, administrative-territorial reform, fight against economic crimes and corruption, rapprochement with Transnistria.

All these circumstances are so evident that the President V. Voronin at the last in 2003 session of the Government (24.12.2003) pointed out that "programme goals of the Government are fully not realized and instruments stipulated for by the government action programme "Revival of economy – revival of the country" are not used to the right degree".

Look from outside

Moldova from the outside is perceived as a country, where due to the inertia of the 90's, but through other methods, "survival policy" is still realized and that does fail to activate factors of sustainable economic growth.

The Government admits the same by implication through its forecast for 2004-2006 of a GDP growth reduction to 5.0% as compared to 6-8% GDP growth achieved during the last two years, while international organizations and rating agencies' forecasts even lower – only 3.5-4.0%. Such rates cannot solve anything indeed. After all our GDP per capita (460-500 USD) today is the level of such exotic African countries as Senegal, Cameroon or Ghana. And in this situation Republic of Moldova, the poorest European country really needs a breakthrough in economic policy, consent between the government and the society on composition, rates and order of transformation of the country's economy.

We aspire to enter Europe. So here is a look from that direction at our starting position: "due to insufficient work of administrative machinery and lack of an efficient democratic control over the former Moldova's economy encounters high level of corruption, informal sector making up almost 80%, which is why incomes from taxes are being lost; there is no control over the eastern border of the country and its social system is insufficient" (Resolution of the European Parliament on Moldova, 18.12.2003).

What's next?

Unfortunately, 2004 is another pre-election year and, of course, there will be a lot of PR-economy and promises. One could, nonetheless, insist that the country's economy had already adapted to market conditions and therefore growth inertia has already emerged, and given all risk factors no one should expect any force majeure events (as a default) during the new year. There are encouraging signs that, economic policy will finally become intelligent and, according to Marian Lupu, Minister of Economy, we in for a "year of active actions" combined into five "baskets": macroeconomic conditions for implementation of structural reforms; raising of competitive economy's potential; social policy; elimination of infrastructural restrictions; state management system reform.

The latter is especially important. During the nearest years it will be modernization of state bodies under the European standards, raising of the society's confidence in the state that will be of decisive importance, rather than so-called market reforms.